DOC could use the daily market exchange rate for every day of the investigation, but such a procedure would have problems of its own. Minor exchange rate fluctuations occur frequently. Foreign firms cannot be expected to change their U.S. price on a daily basis to keep up with such fluctuations. To do so would prevent the use of any kind of published list price or the use of the price in advertising. Furthermore, pricing decisions are generally made as parts of long-term strategies, in which case a foreign firm would consider the average exchange rate it expects to prevail over the planning period when making its pricing decisions. Many firms invest considerable time, resources, and advertising money in developing market share and market goodwill. They are not likely to want to give that up by raising their prices to reflect a change in the exchange rate that they view as a temporary aberration.

DOC recognizes these problems at least to some extent. It gives firms up to 90 days to recognize changes in the exchange rate as being permanent and reflect them in their prices. It also makes allowances to ensure that temporary spikes in the exchange rate do not result in findings of dumping. One may argue that these measures are not adequate to take care of all problems in this regard, but they do take care of some of the more egregious ones.

The problem of choosing the correct exchange rate for dumping calculations is difficult, if not intractable. No one rate is valid for all firms and industries because the cost of gaining and losing market share varies from industry to industry. Further, whether the current exchange rate at any given time is permanent or a temporary aberration (and, if an aberration, how far out of line with the permanent rate it is) is subject to opinion and cannot be answered objectively. Probably the best that can be done is to pick a reasonable methodology--such as an average of the exchange rates over several quarters--and then set the *de minimis* level of dumping high enough that firms that use other reasonable methodologies in their business transactions are not found guilty of dumping simply by virtue of that fact. DOC's exchange rate policy is questionable, although it makes some attempt at ameliorating some of the more egregious problems that can occur. The *de minimis* level of dumping, however, is not set high enough to eliminate problems.

Setting *De Minimis* Levels of Dumping

The *de minimis* level of dumping set by DOC--that is, the level above which dumping is considered to exist and below which *no* dumping is considered to exist--is 0.5 percent of the U.S. price of the import. That level has two problems. First, dumping at even twice this margin is highly unlikely to injure U.S. firms at all. Successful predatory pricing would probably require at least 20 times this margin. One might argue that determining injury is the function of the ITC, not DOC. A finding of dumping allows a case to continue, however, thereby continuing the burden on the foreign firm that was discussed above.

A second problem with the low *de minimis* level is that DOC is often unable to determine dumping margins within an error of 0.5 percent. Many products are produced by multiproduct firms. Such firms have overhead costs that are relevant to all products and for which opinions can differ as to how much should be allocated to each of the various products. Similarly, such firms often engage in research producing results that are used in several products, and there is no objective answer to the question of how much of the research costs should be attributed to various products in a dumping investigation. Estimates of depreciation rates and rates of obsolescence are very rough and subject to opinion. How these and many other questions are handled are often dictated by accounting standards that vary from country to country.

With all of these problems, DOC is unlikely to be able to determine dumping margins reliably within an accuracy of several percentage points, much less 0.5 percent. Recall that the exchange rate methodology used by DOC can produce errors as large as 5 percent, which is 10 times the *de minimis* margin.

How the Process Works for Nonmarket Economies

The problem is much worse for cases involving countries with nonmarket economies. In market economies,

the price of a good or service tends to reflect the true cost to the economy of producing it. That is not the case in a nonmarket economy, however, where administrative fiat determines prices. Hence, the cost of producing a product in a nonmarket economy cannot be calculated by adding up the various inputs multiplied by their respective prices. To find the cost, DOC multiplies the quantities of the various inputs used in the country in question by the prices of the respective inputs that prevail in another country that has a market economy, thereby obtaining costs for the various inputs. It then adds up those calculated input costs to obtain the total cost.

That procedure may be the best that can be devised to determine dumping in a nonmarket economy. Yet even at its best--when DOC uses a country with a similar level of development, similar resources, and the like--the procedure is not very accurate. Different countries have different tariff structures, which causes the prices of various goods and services to differ in ways that are too complicated to sort out without detailed models of the economies. Furthermore, different cultures in different countries lead to different patterns of consumption and production, which in turn lead to different prices. In short, even countries that appear to be similar are likely to have significant differences.

In practice, the procedure is often not at its best. Frequently, no market economy similar to the economy under investigation exists, or DOC chooses not to use the most closely similar countries because those countries too are under investigation. Further, the choice of the most similar country has a large element of subjectivity to it, leaving room for DOC to choose a country that would make the dumping margin look large. In some cases, the comparisons have been strained. For example, Robert A. Cass and Stephen J. Narkin report that with the criteria of similar economic structure and similar level of development:

> It would be hard to find (as Commerce has found) that a combination of the Federal Republic of Germany, Japan, France, Canada, Switzerland, and the Netherlands represents a good surrogate for the People's Republic of China or that the United Kingdom or the Federal Republic of Germany are suitable surrogates for the Soviet Union.[10]

In those cases, the surrogate countries are much more developed than the countries being investigated, which means that wages are much higher in the surrogate countries than in the investigated countries. Those higher wages are especially important when one considers that the low wages in the investigated country encouraged the use of less labor-saving capital and more labor than the higher-wage surrogate country would use.

The Commerce Department has argued that the choice of surrogates described in the quotation above could no longer occur because of changes in laws and procedures. Such changes, however, cannot create good surrogate countries when good surrogate countries do not exist. Further, though properly chosen rules could limit the subjectivity involved in picking a surrogate country, it would be difficult if not impossible to eliminate the subjectivity without imposing rules that sometimes lead to bad choices.

How Industries Are Defined

How an industry is defined is important for determining whether or not dumped and subsidized imports cause material injury. Import competition might substantially curtail narrowly defined parts of an industry while the industry as a whole remains healthy and uninjured. If the industry is defined to consist solely of those narrow parts, the ITC is much more likely to find that the imports cause material injury.

An example of that problem is the series of cases concerning fresh cut flowers, which will be discussed in more detail below. In cases where the flower industry as a whole or broad segments of it were at issue, the ITC usually found no injury. When the domestic industry later filed cases for specific flowers, the ITC did find injury. It is not unusual for antidumping and countervailing-duty orders to apply to products that are clearly only a small part of the output of what most people would think of as an industry. For example, one current antidumping order applies to chrome-plated lug nuts but not other varieties.

10. Ronald A. Cass and Stephen J. Narkin, "Antidumping and Countervailing Duty Law: The United States and the GATT," in Boltuck and Litan, eds., *Down in the Dumps*, p. 216.

Applying Retrospective Duty Assessment

The retrospective nature of the U.S. system of antidumping and countervailing duties introduces uncertainty that makes the duties more protective than they would appear. A firm importing goods under an AD/CVD order does not know how much it will ultimately owe in duties.

At the time of import, the firm pays an estimated duty equal to the dumping or subsidy margin determined in the AD/CVD investigation or, if there has been one, the last administrative review. If an administrative review occurs before the imports are liquidated (that is, before the final paperwork on duties owed is completed), however, the firm may find that the actual dumping or subsidy margin for the imports in question was either larger or smaller than the estimated duty paid. If it was larger, the importer will have to make up the difference. To reduce its exposure to this risk, the importing firm is likely to reduce imports of the product from the exporter in question and switch to a different supplier.

Using Administrative Proceedings

As was discussed in Chapter 3, dumping was once a criminal offense tried in a court of law and subjecting violators to fines, imprisonment, and civil suits. Now, however, both antidumping and countervailing-duty cases are decided administratively and involve added duties on the imports rather than criminal and civil penalties.[11] Although cases can be appealed to the Court of International Trade, and from there to the Court of Appeals for the Federal Circuit, the administrative and noncriminal nature of the cases means that the U.S. government has greater latitude in the procedures it can use in determining dumping. As a result of that greater latitude, a firm accused of dumping may find it more difficult to defend itself successfully.

Viewed from the perspective of the AD/CVD laws as an alternative to the escape clause, the change from courts and punishment to administrative agencies and duties is entirely appropriate. DOC and the ITC are more knowledgeable about trade and U.S. industries and their need for protection than are the courts. Moreover, since the emphasis is on protecting U.S. industries rather than deciding the guilt and punishment of foreign firms for misdeeds, there are no defendants and no need for courts to protect defendants' rights.

Clearly, however, though foreign exporters are not subject to criminal conviction and punishment under current AD/CVD law, they are harmed by antidumping and countervailing duties, lending credence to the view that protections similar to those of the criminal law should be maintained. From the perspective of the AD/CVD laws as preventing, punishing, and offsetting the effects of predatory pricing or other unfair trade practices, some of the procedures that have evolved appear unfair and likely to introduce bias against foreign exporters and U.S. consumers.

Decisions Are Made by an Advocate of One Side in the Case

The Office of Investigations in DOC effectively serves as investigator, prosecutor, judge, and jury in dumping and subsidy determinations. It investigates the firms in question--sometimes on its own initiative--and makes the determination of dumping or subsidy. Not even an administrative law judge separate from the investigators makes the decision.

Further, as was discussed in Chapter 3, DOC is expected to be an advocate of U.S. business in general. Thus, DOC, which plays the role of judge in AD/CVD cases and therefore should be neutral, is actually an advocate of one of the parties to the cases. The problem is made more serious by the requirement in the Trade and Tariff Act of 1984 that the agencies administering the AD/CVD laws give technical assistance to small firms desiring to file petitions for relief.

11. That is true provided the cases do not involve predatory intent and therefore are not being pursued under the Antidumping Act of 1916. See Chapter 3.

Some Firms Are Assumed to Be Dumping Until Proven Otherwise

When the number of firms in an antidumping case is so large as to strain its resources, DOC investigates a sample of the firms rather than all of them. For the sample, DOC typically starts with the firm with the largest market share, proceeds to the firm with the next largest share, and so on until it has chosen enough firms to cover 60 percent of the imports in question. For each investigated firm for which the determinations of dumping and injury are positive, an antidumping duty equal to the dumping margin found in the investigation is imposed. Then, an antidumping duty equal to the weighted average of the duties on all the investigated firms is imposed on the firms that were not investigated.

In calculating the weighted-average duty to be applied to uninvestigated firms, DOC, for reasons that are unclear, leaves out all zero and *de minimis* margins found on investigated firms, thereby increasing the calculated average. If one or more of the investigated firms fails to provide information requested by DOC, however, and DOC consequently uses the best information available, the resulting dumping margin determined for that firm is included in the average.

Uninvestigated firms can voluntarily provide information during the investigation and thereby get an individual dumping margin determined. Since DOC chooses the firms with the largest market shares, however, the uninvestigated firms are likely to be the smaller firms that find the cost of meeting DOC's information demands to be the most onerous.

Subsequent administrative review will determine whether each uninvestigated firm is indeed dumping. For each firm that is not, the estimated duties paid will be returned with interest. That does not eliminate the damage to those firms, however. Because the U.S. importer, rather than the foreign exporter, pays the estimated duties, the importer is not likely to know whether the exporter is dumping and therefore would have to assume that the estimated duties might not be refunded. Consequently, it would probably reduce imports of the good from the firm in question and switch to another supplier. Refunding deposits of estimated duties after an administrative review found them unjustified would not restore the sales lost before the review. The firm could lower the price to try to keep from losing the sales, but doing so would virtually guarantee that the administrative review would find dumping.

The sampling procedure effectively means that in cases where both DOC and a defendant firm find an investigation to be too expensive and troublesome to undertake, the firm is assumed to be dumping and punished at least until the first administrative review. That practice is a reversal of what occurs in criminal trials, in which people are assumed innocent until proven guilty, and in civil suits, in which plaintiffs must win in court before receiving monetary damages.

The sampling procedure also punishes uninvestigated firms for the dumping other firms commit. Including cases that involve BIA punishes uninvestigated firms for the failure of investigated firms to comply with DOC's demands for data.

Clearly, from the perspective of antidumping and countervailing duties as punishment of foreign firms for unfair trade and as offsets of the effects of unfair trade, the sampling procedure is unreasonable. If, however, the purpose of the duties is not to punish the foreign firms but to protect domestic industries from intense competition without regard to fairness, the procedure would seem no different than ordinary tariffs and quotas.

Cases Can Be Used as Harassment Against Foreign Firms

In criminal trials, if a defendant is found innocent, the prosecutors cannot bring charges again for the same offense. In trade remedy cases, that prohibition does not provide much protection: each time a given good is imported represents a possible new offense, and several different laws can be used to obtain protection. As long as a good continues to be imported, nothing can stop the domestic industry from trying over and over again to obtain protection under the trade remedy laws.

The industry has several incentives to do just that. First, by using different laws (Section 201 escape clause, antidumping law, countervailing-duty law, and the like) and trying different tactics each time, the industry may eventually hit upon a tactic that succeeds in

getting protection. Furthermore, over time the personnel on the ITC or at DOC may change, possibly resulting in more sympathy for the domestic industry.

Second, repeated cases are expensive for the defending foreign exporters to deal with. The costs of complying with the Commerce Department's requests for information and of hiring U.S. legal help have already been discussed. Moreover, the bias in DOC's methodology and the low *de minimis* threshold it uses mean that a foreign firm is apt to be found to be dumping by at least a small amount.

The foreign firm having been determined to be dumping, the problem of retrospective duty assessment and resulting periods of uncertainty then kicks in. At least until the ITC's final determination of injury, and continuing after that determination if it is positive, imports will not be liquidated until sometime after they enter the country, meaning that the importer does not know the antidumping duty for sure until after it has imported the good. Thus, repeated filing of cases--even if none of the cases result in antidumping or countervailing duties--can be an effective form of harassment of foreign exporters by the domestic industry. They can hinder the imports and persuade the exporter to cease exporting to the United States, raise its prices, or enter into a "voluntary" restraint agreement.

An example is provided by the case of fresh cut flowers.[12] In the 1970s and 1980s, Colombia emerged as a major supplier of fresh cut flowers to the United States. For reasons of climate, soil, and an abundance of low-wage, unskilled labor, Colombian costs in 1970 were 31 percent lower than U.S. production costs, even after factoring in the higher transportation costs. In addition, Colombia's climate allowed growth of flowers without greenhouses during U.S. winter months for such high-flower-sales days as Valentine's Day, Easter, Christmas, Secretary's Day, and Mother's Day.

The growth of imports led U.S. growers to seek protection in 1977 under the Section 201 escape-clause provision of U.S. law. Recall from Chapter 1 that this provision provides for temporary protection from imports regardless of whether they are fairly or unfairly traded, but the imports must be a "substantial cause of serious injury" to the domestic industry. The ITC ruled against the domestic industry. The industry tried again under Section 201 in 1979, and the ITC once again ruled against it.

In the 1980s, the industry tried antidumping and countervailing-duty cases. From 1980 to 1985, it had only limited success in attempting to protect rose growers. A case concerning all cut flowers in 1986 resulted in a determination that Colombian exporters were being subsidized at rates of 4 percent to 5 percent. The Colombian growers agreed not to receive the subsidies, so no duties were applied. Then the domestic industry changed strategy, switching from protection for the industry as a whole or broad segments of it to protection for narrowly targeted segments. In 1986, the industry filed antidumping and countervailing-duty cases against seven types of flowers from 10 countries.

Those cases finally resulted in a number of favorable rulings from DOC and the ITC, and the industry finally received protection after failing many times before. All told, through 1989, 49 unfair import investigations took place concerning fresh cut flowers, 14 of them against Colombian exporters. One can find a similarly protracted history of repeated investigations and appeals relating to consumer electronics beginning in 1959 and extending over 20 years (see Table 2).

Setting AD/CVD Duties to Protect U.S. Firms

In the defense of antidumping and countervailing duties, analysts sometimes argue that they raise the prices of the goods in question back up to where they would be if the dumping or subsidies did not occur, thereby restoring the proper free-market result, which is thought to be optimal.

Some of the fallacies of this argument are evident from previous discussion in this study: dumping is a normal free-market result, both dumping and subsidies by foreign exporters and governments are economically beneficial to the U.S. economy as a whole, and raising the prices back to undumped and unsubsidized levels is

12. José A. Mendez, "The Development of the Colombian Cut Flower Industry: A Textbook Example of How a Market Economy Works," in J. Michael Finger, ed., *Antidumping: How It Works and Who Gets Hurt* (Ann Arbor, Mich.: University of Michigan Press, 1993), pp. 115-116.

Table 2.
History of Consumer Electronics Import Litigations, 1959-1979

Year	Complaint	Agency	Administrative and Judicial Action	Related Diplomatic Action
		Radios		
1959	Transistor radio imports from Japan posed a threat to U.S. national security		Case dismissed, May 1962, after two and a half years of investigations	Japanese government imposed voluntary export quotas on transistor radios to the United States
		Components		
1961	TV tube dumping	Treasury	No dumping found	
1964	TV tube dumping	Treasury	No dumping found	
1970	Fixed resistor, transformer, and capacitor dumping	Treasury	No dumping found	
1970	Tuner dumping	Treasury	Dumping found	
1972	TV tube dumping	Treasury	No injury to the U.S. industry found	
		Television Receivers		
1968	Monochrome and color TV receiver dumping	Treasury	Dumping found, March 1971. Dumping duties imposed retroactively, mid-March 1978	
1971	Escape-clause action claiming injury to the U.S. television industry	Tariff Commission	Case dismissed	
1970-1972	Three separate complaints, claiming that exports of Japanese color TV and other consumer electronic products were subsidized, resulting in injurious trade distortions	Treasury	Case dismissed, with negative determination	
1974	Antitrust violations by Matsushita Electric with the acquisition of Motorola's TV division	Justice	Acquisition not opposed	
1974	Violation of antitrust and antidumping laws	U.S. District Court, Philadelphia	Case pending (as of October 26, 1979)	

Table 2.
Continued

Year	Complaint	Agency	Administrative and Judicial Action	Related Diplomatic Action
		Television Receivers (Continued)		
1976	Appeal against the Treasury Department's ruling on export subsidies	U.S. Customs Court, New York	Unanimous decision that commodity tax rebate constitutes export subsidy calling for CVDs	
1977	Appeal against U.S. Customs Court decision	Court of Customs and Patents Appeals and U.S. Supreme Court	U.S. Customs Court decision reversed	
1976	Unfair trade practices, including subsidies for color TV exports and dumping	ITC	Reversal of U.S. Customs Court decision upheld and Treasury Department's dismissal of the case sustained	
1976	Allegations of 14 unfair trade practices coming within the scope of the AD, CVD, and antitrust laws	ITC	"No contest" consent order, under which the ITC would monitor Japanese pricing practices in the United States	
1976	Escape-clause action, seeking to impose import quotas on grounds of injury to the U.S. television industry	ITC	Case dismissed. Recommendation to the President that higher import duties be imposed on color televisions to protect an injured U.S. industry. Recommendations were rejected by the President after conclusion of the Orderly Marketing Agreement	Orderly Marketing Agreement signed between Japan and the United States, under which Japan agreed to limit color TV exports to the United States to 1,750,000 sets annually
		Microwave Ovens		
1979	Microwave oven dumping	Treasury and ITC	The Treasury requested the ITC to rule on the effects of imports of microwave ovens from Japan; the ITC found injury. Dumping investigation by the Treasury under way	

SOURCE: Gene Gregory, "The Profits of Harassment," *Far Eastern Economic Review* (October 26, 1979), pp. 74-79.

NOTE: CVDs = countervailing duties; ITC = International Trade Commission; AD = antidumping.

economically harmful to the U.S. economy as a whole. Even if that were not the case, however, the antidumping and countervailing duties stipulated by U.S. law are larger than they should be to restore the prices that would prevail if there were no dumping or subsidies. Hence, they result in prices that are higher than would prevail if there were no dumping or subsidies, and they thereby protect domestic industry at the expense of the consumer.

In the case of dumping, the reason that the U.S. price is lower than the foreign home-market price is normally (barring a recession in the United States) that the foreign exporter has a greater degree of monopoly power in its home market and is therefore able to charge a higher price than it could in a competitive market. Thus, at least part of the dumping margin, and possibly all of it, results from high prices in the home market and not from low prices in the U.S. market. Hence, the firm could charge a lower price in the home market and still make a profit there.

If the firm was prohibited from dumping, it most likely would do just that. It would eliminate the dumping margin partly by raising its U.S. price and partly by lowering its home-market price. The U.S. price would thus rise by only part of the dumping margin. The antidumping duty imposed by the United States, however, by law must be equal to the entire dumping margin--not just the amount by which the U.S. price would be higher if the foreign firm was prohibited from dumping. Hence, the antidumping duty raises the U.S. price higher than prohibiting dumping would.

Countervailing duties are also frequently too high in the case of production subsidies and subsidies on exports to all countries, at least in the case of competitive industries (see Box 3). Whether they are too high in cases of imperfectly competitive industries is unclear, but DOC makes no attempt (and the law does not allow it) to calculate the proper level of countervailing duty to offset the subsidy exactly.

Regarding limits on the size of antidumping duties, Article VI of the GATT says, "In order to offset or prevent dumping, a contracting party may levy on any dumped product an anti-dumping duty not greater in amount than the margin of dumping in respect of such product." The Antidumping Code says, "It is desirable . . . that the duty be less than the margin, if such lesser duty would be adequate to remove the injury to the domestic industry."

Regarding limits on the size of countervailing duties, Article VI holds, "No countervailing duty shall be levied . . . in excess of an amount equal to the estimated bounty or subsidy determined to have been granted. . . ." The Subsidies Code states, "It is desirable . . . that the duty be less than the total amount of the subsidy if such lesser duty would be adequate to remove the injury to the domestic industry."

Thus, U.S. antidumping and countervailing duties are in accord with the requirements of GATT Article VI and the Antidumping and Subsidies Codes. They are not in accord with what the codes say is desirable, however. The duty is always equal to the margin of dumping or subsidy, even when lesser duties would be adequate to remove any injury to the domestic industry.

Determinating Whether Subsidies Are Specific

The United States does not countervail subsidies generally available to all industries, but rather only those that, according to economic theory, affect trade. DOC, however, has some questionable policies for determinating what is a specific subsidy and what is a generally available subsidy.[13]

In particular, DOC considers regional subsidies--such as regional development programs, urban block grants, and regional job training programs--to be specific subsidies no matter how widely available they are to industries in the region, and it considers general agricultural subsidies to be nonspecific. Those classifications are wrong, and they conveniently exempt the largest U.S. subsidy programs affecting trade--those in agriculture--from countervailing duties while allowing the United States to impose duties against subsidies that are more commonly used by other countries.

13. For the most part, this section of the chapter consists of arguments and examples from Joseph F. Francois, N. David Palmeter, and Jeffrey C. Anspacher, "Conceptual and Procedural Biases in the Administration of the Countervailing Duty Law," in Boltuck and Litan, eds., *Down in the Dumps*, pp. 98-99.

Box 3.
Why the Countervailing Duty More Than Offsets the Subsidy in Cases of Competitive Markets

Suppose that a foreign country subsidizes one of its industry's exports to the United States and a third country, that the subsidy is proportional to the value of the exports in question, that the industry is competitive so that no one firm can significantly affect the market price in any country, and that the firms in the industry have increasing marginal and average costs--that is, increases in a firm's output cause its marginal and average cost per unit of output to increase--as is often the case in the real world.[1]

That situation can be analyzed as the superimposition of two cases: one in which the country subsidizes its industry's exports to the third country but not the United States, and one in which the country subsidizes its industry's exports to the United States but not the third country. In both cases, one must assume that no trade is allowed between the other country and the United States in order to keep subsidized exports to one country from being reexported from that country to the other and thereby undercutting the unsubsidized exports to the second country. This requirement disappears once the cases are superimposed because exports to both countries are subsidized.

Examine first the case in which the foreign country subsidizes its industry's exports to the third country but not its exports to the United States. The subsidized exports to the third country would increase those exports, which would increase the outputs of the firms in the industry and therefore increase their marginal and average costs. The increase in marginal cost would cause the firms to increase the price they charge on exports to the United States (since firms set price equal to marginal cost for profit maximization in unsubsidized markets), and this price increase would decrease the quantity of those exports. Thus, the subsidy on exports to the third country increases the price and decreases the quantity of exports to the United States.

Examine next the case in which the foreign country subsidizes its industry's exports to the United States but not to the third country. The subsidy would lower the price and increase the quantity of exports to the United States if it was not countervailed. U.S. law, however, stipulates a countervailing duty exactly equal to the subsidy margin. Such a subsidy would exactly offset the decrease in price and therefore restore both the price and quantity of exports to their unsubsidized levels.

Finally, superimpose the two cases to obtain the situation of interest: where the foreign country subsidizes its firms' exports to both the United States and the third country. The subsidy on exports to the United States decreases their price and increases their quantity. The subsidy on exports to the third country raises the price of exports to the United States and lowers their quantity, which partially offsets the effect of the subsidy on exports to the United States. Recall from the second case above that the countervailing duty alone is large enough to offset completely the subsidy on exports to the United States. Thus, the countervailing duty plus the effects of the subsidy on exports to the third country together more than offset the effects of the subsidy on exports to the United States. In other words, in this case the countervailing duty stipulated in U.S. law is too large: it more than offsets the net effects of the subsidy on exports to the United States.

The same is true of a production subsidy, but the effect is even larger. A production subsidy effectively subsidizes domestic sales of the subsidizing country as well as exports to the United States and other countries. Thus, both domestic sales and exports to the third country increase, thereby increasing the marginal costs of the producers. Those higher marginal costs result in higher prices for and lower quantities of exports to the United States, which partially offset the lower prices and higher quantities that result from the portion of the production subsidy that subsidizes exports to the United States. Once again, the U.S. countervailing duty is large enough to offset this portion all by itself and therefore is too large when all of the effects are netted out.

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1. The argument presented here is taken from Richard Diamond, "Comment," in Richard Boltuck and Robert E. Litan, eds., *Down in the Dumps: Administration of the Unfair Trade Laws* (Washington, D.C.: Brookings Institution, 1991), pp. 141-151.

In DOC's defense, one can say that if it considered otherwise nonspecific regional subsidies to be specific, an exporting country could abuse the policy by granting a subsidy to all firms in a region whose geographic boundaries were carefully tailored to include only a particular industry. It would seem, however, that DOC could use its subjective judgment to make exceptions for such cases, just as it already uses its subjective judgment to make exceptions for cases in which subsidies by law are nonspecific but appear in practice to go only, or disproportionately, to certain industries.